The Obviousness of Anarchy: Internalizing Externalities - The Art of Not Being Governed

by John Hasnas, Associate Professor, Georgetown University, J.D., Ph.D, LL.M.

Continued from ***The Obviousness of Anarchy: Police***

Supporters of government often argue that government is essential to provide needed regulation of market activities. Individuals contracting with each other in a market often act in ways that impose harm or unconsented to costs on others. Manufacturers make and consumers purchase products whose use imposes an unacceptable risk of injury on third parties.

For example, automobile companies can produce and drivers will purchase cars that can move at speeds or have handling properties that create an unreasonable risk of injury to pedestrians. Oil companies can ship oil to consumers in ways that create an unreasonable risk of spills that would pollute the land or body of water over which the oil is transported. More generally, because people do not bear the costs their activities impose on others, they will often act in ways that impose greater costs on society than are justified by the personal benefits they realize. These unconsidered costs to others are the social costs of market activity; what economists call *negative externalities*.

rules not rulers

Supporters of government contend that only government can regulate market activity to ensure that private contractors consider the social costs of their transaction. Thus, even if rules of law, courts, and police services could be supplied non-politically, government would nevertheless be essential to internalize externalities.

I must confess that I am at a loss as to how to respond to this argument. Look around is not enough. That this argument has any plausibility at all is a testament to how completely oblivious people can be to the world around them. In a world in which one of the dominant political issues is tort reform; in which businesses are continually complaining to Congress that they are over-regulated by the common law of tort and begging government to protect them from this non-political method of internalizing externalizes, how can anyone seriously assert that government regulation is needed to deal with the problem of social costs?

It is true that economists posit a fictitious realm in which human beings engage in voluntary transactions free of all forms of regulation. But they do so because such an idealized conception of the market is useful to their exploration of the science of human interaction in much the same way that the concept of a perfect vacuum is useful to physicists exploring the laws of nature; not because they think it corresponds to anything in reality. In the real world, human interaction is always subject to regulation; by custom, by people's ethical and religious beliefs, and, in our legal system, by the common law. Tort law is precisely that portion of the law that evolved to protect individuals' persons and property from the ill-considered actions of their fellows, that is, to internalize externalities. It is only by ignoring the existence of these forms of non-political regulation, that is, only by believing that the economists' model of the market is a description of reality, that one could possibly believe that government is necessary to address the problem of social costs. Of course, one should never underestimate the power of a conceptual model to blind intellectuals to what is going on in the real world.

But, supporters of government claim, common law can never be an adequate regulatory mechanism

because it is necessarily retroactive in operation. Lawsuits arise only after harm is done. Therefore, civil liability could never provide the type of proactive regulation necessary to prevent serious harm from occurring. Really? The basic rules of tort law prohibit individuals from intentionally harming others and require them to act with reasonable care to avoid causing harm inadvertently. There is nothing retroactive about this. It is true that precisely what constitutes reasonable care may have to be determined on a case by case basis, but in this respect, the common law is no different than government legislation that announces a general rule and then leaves it up to the courts to determine how it applies in particular cases.

Furthermore, the common law can act prospectively in appropriate cases. The injunction, an order not to engage in a specified activity, evolved precisely to handle those cases in which one party's conduct poses a high risk of irreparable harm to others. **[28]** And by the way, government legislation is almost always retroactive as well.

Limitations on human knowledge (not to mention public choice considerations) mean that legislators are rarely able to accurately anticipate future harm. Megan's law required public notification when a known sex offender moves into a community. It is called Megan's law because it was enacted after Megan was killed by a repeat sex offender who lived in her community. If I remember correctly, Sarbanes-Oxley was passed after Enron collapsed. And when was the USA Patriot Act passed? Oh, yes, after 9/11.

Until 1992, fast food restaurants served coffee at between 180 and 190 °F, a temperature at which the coffee can cause third degree burns in two to seven seconds if brought into contact with human skin. This posed a considerable risk of serious injury, given how often coffee served in styrofoam cups is spilled. I did not notice any proactive legislative regulation designed to internalize this externality.

In 1992, Stella Liebeck won a judgment against McDonald's for injuries received when she spilled coffee on herself equal to her medical expenses plus the amount of profit McDonald's earned in two days from knowingly selling coffee at a dangerously high temperature. **[29]** The next day every fast food restaurant in the United States served its coffee at 158 °F, a temperature at which it takes 60 seconds to cause third degree burns; a sufficient amount of time for customers to brush the coffee off their clothes or skin. There may be many things wrong with contemporary tort law, **[30]** but being ineffective at internalizing externalities is most assuredly not among them.

The only way to believe that government is necessary to resolve the problem of social costs is to be studiously blind to the nature of both common law and government legislation.

Continued in ***The Obviousness of Anarchy: Public Goods***

Footnotes

[28] Note that to obtain an injunction at common law and thereby curtail another citizen's freedom, one must meet a very high evidentiary threshold by establishing a high likelihod of irreparable harm. This is in contrast to government legislation that can curtail citizens' freedom whenever the politically dominant faction of the legislature deems it necessary, even if only to effectuate the "precautionary principle." I leave it to the reader to decide which is the superior standard for addressing potential future harm.
[29] The judgment was reduced by 20% to take account of Ms. Liebeck's contributory negligence with regard to how she opened the cup. This amount was further reduced on appeal.
[30] Almost all of which are attributable not the way it evolved at common law, but to twentieth century efforts to improve upon the outcome of this evolution. See John Hasnas, What's Wrong with a Little Tort Reform? 32 IDAHO LAW REVIEW 557 (1996).

,,

1. i love this series. thanks for posting!

Reply

Your email address will not be published.

You may use these HTML tags and attributes: `<a href="" title=""> <abbr title=""> <acronym title=""> <b> <blockquote cite=""> <cite> <code> <del datetime=""> <em> <i> <q cite=""> <s> <strike> <strong>`